United States Court of Appeals

for the Second Circuit

APPELLANT'S REPLY BRIEF

ORIGINAL

74-2326

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

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In the Matter of

D.H. OVERMYER CO., INC. (Florida
D.H. OVERMYER CO., INC. OF OHIO
D.H. OVERMYER CO., INC. (Colorado)
D.H. OVERMYER CO., INC. (New York)

Debtors-Appallants,

-and-

ROBERT P. HERZOG,

Receiver-Appellant.

----------x

In Proceedings for
An Arrangement
No. 73 B 1134
No. 73 B 1128
No. 73 B 1131
No. 73 B 1151

B
P/S

ON APPEAL FROM THE UNITED STATES
DISTRICT COURT FOR THE SOUTHERN
DISTRICT OF NEW YORK

REPLY BRIEF OF RECEIVER-
APPELLANT WITH RESPECT TO
BUFFALO 2
COLUMBUS 3
DENVER 4
MIAMI 7-9

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REPLY BRIEF OF RECEIVER-APPELLANT WITH RESPECT TO BUFFALO 2, COLUMBUS 3, DENVER 4, AND MIAMI 7.

Preliminary Statement

The landlords of the four subject warehouses are represented by a single attorney who has submitted a single principal brief in opposition to the brief of the Receiver-Appellant. The within brief of the Receiver-Appellant is submitted in reply and addresses itself to the four proceedings in question. In two of these cases (Columbus 3 and Denver 4) the landlords do not rely on the bankruptcy default clause.

At the outset it must be noted that the brief of the landlords herein goes beyond the scope of the record in two respects.

The landlords state that the Receiver, "though doing an admirable job...was approximately two months behind in use and occupation (or rent) payments..." (landlords' brief, p. 23). There is no authority for this statement in the record and it is simply not true that the Receiver is two months behind in use and occupation payments.

At page 13 of landlords' brief the statement is made that a Denver 4 subtenant has moved out thereby reducing the monthly rent roll to $10,102.00 This statement is grossly improper. The landlords have been in possession of the buildings since October 15, 1974, and there is no indication when the subtenant allegedly moved, whether the move was the result of any action by the landlords, whether the subtenant has been replaced, whether it is anticipated that a higher rental will be received on a re-letting, and so forth. Nor should there be inasmuch as such events, occurring long after the trial, have no place on appellate review.

If the Receiver were to resort to the same tactics he could easily establish that subsequent to the trial of Miami 7, the Miami 7 warehouse became a highly profitable building although, as is noted in Schedule A to the Brief of

Receiver-Appellant, this profit does not appear from the record.

In their remaining legal arguments the landlords lump together all four buildings and further make general reference to the other proceedings herein. Under these circumstances a capsule review of the earnings of these buildings is in order.

Warehouse	Pre-Petition Arrears	Annual Net Profit	Remaining Term of Lease Including Renewals
Buffalo 2	$14,187	$43,888	33 years
Columbus 3	$15,505 (However, landlord elected to terminate solely on basis of default in payment of taxes and interest aggregating $5,185.10)	$15,232	24 years
Denver 4	$16,100	$23,200	33 years
Miami 7	$33,306	*	38 years

*As is noted above, the profitability of Miami 7 does not appear from the record. However, the testimony at the trial on January 31, 1974, establishes that the single tenant occupying the entire warehouse was paying a rental of $1.09 a square foot per annum under a lease expiring May 31, 1974. The manager for the Receiver testified that the going market rate for comparable warehouse space in the area was between

$1.45 and $1.50 a square foot per annum. (L-8).

With respect to the alleged lack of repairs, a part of the "pattern of consistent failure" found by the District Judge (15), the actual facts are as follows:

Buffalo 2	-	No default asserted by landlord, nor was notice of default given. Debtor expended $30,000 for repairs several months prior to the bankruptcy. (B-11,12).
Columbus 3	-	Uncontradicted testimony at trial was that only repairs required were for "minor" paving at a cost of between $2,500 to $3,000. (D-24,25).
Denver 4	-	No default asserted by landlord, nor was any notice to repair given.
Miami 7	-	The uncontradicted testimony was: "This really is a good building, in very good shape." (L-38).

POINT I

THE REFUSAL OF THE LOWER COURTS TO GRANT EQUITABLE RELIEF CONSTITUTED ERROR.

The landlords attempt to distinguish the doctrine of Queens Boulevard Wine and Liquor Corp. v. Blum, et al., ___F.2d___, Docket No. 74-1512 (2d Cir., filed June 11, 1974), Slip Sheet Opinion at 4113 et seq., from the cases at bar.

The applicability of Queens Boulevard is set forth at pages 86-92 of the First Brief of the Receiver-Appellant (Appellants' Appendix Volume 2) and will not be repeated in this reply brief.

The landlords argue that defaults with respect to the four warehouses at issue range from $18,000.00 to $44,000.00 per property resulting in "serious impedence". This is contrasted with Queens Boulevard where there was only a one month rent arrears and a security deposit which could be applied in payment of same. (Landlords' brief, p. 23).

The testimony at the trials established that pre-petition defaults with respect to the four warehouses range from $14,000.00 to $33,000.00 and while the difference between these amounts, and the larger sums cited by landlords, will not be dispositive of the significant issues on this appeal, it does underscore the difficulty of attempting to rely on alleged findings which simply do not exist. The parties in these and all of the other proceedings draw conflicting conclusions from the same record, putting this court in the burdensome position of having to choose between them. This result would have been obviated had the Bankruptcy Judge made special findings of fact.

Nor do the landlords treat the amount of the pre-

petition arrears in the context of the profitability, and monthly rent, of each warehouse. Thus, in Buffalo 2 rent arrears of $14,187 00 represent only one and one half months rent payments. This is hardly a distinguishable difference from the one months rent arrears in Queens Boulevard, particularly in light of the fact that Appellants earn an annual net profit of $43,888.00 from the Buffalo 2 property under a lease with a remaining life of 33 years.

The annual profits from the New York debtors leasing operations from the Buffalo 2 warehouse, even over a short period, will far exceed the value of the one month security deposit which existed in Queens Boulevard, or the one and one half months past due rent under the Buffalo lease.

In this regard the landlord of Denver 4 testified that he would reject a tender of pre-petition arrears totalling approximately $16,100.00, preferring instead to appropriate unto himself the profits under the lease.

> "THE REFEREE: ...If all monies were to be tendered to you today, would you be content to continue the lease with Overmyer?
>
> "THE WITNESS: No, sir, Your Honor." (F-47).

The landlords' reliance upon the District Judge's purported finding of a "pattern of consistent failure of the debtors to meet its rent, repair, mortgage and tax

obligations" is misplaced.

With respect to the four warehouses at issue, no such consistent pattern has been shown. As appears supra at page 4 there were no defaults with respect to repairs. Similarly, with respect to the Buffalo 2 and Miami 7 proceedings, the landlords' entire case consisted of placing into the record their request for admissions and responding answers of the Appellants. No "pattern of consistent failure" was shown in these proceedings.

The foregoing points up the error of the lower courts in relying upon generalized findings which cannot be indiscriminately applied to each debtor. By applying such generalized findings, the lower courts gave no consideration to contrary facts which clearly show the efforts of these financially troubled debtor-tenants to pay their debts. There was no distinguishing between varying fact patterns in the different proceedings. There was no recognition by the courts below that the so-called adverse findings do not apply to each debtor. (See Brief of Receiver-Appellant at 71-76).

There were some 40 separate plenary proceedings before the Bankruptcy Judge, 15 of which are now before this Court; and while it is understandable that the probative facts of one might be confused with the naked allegations of another,

and while it is tempting to minimize judicial energies by lumping all cases together, it is just not consistent with the high standard insisted upon by this Court in the landmark case of United States v. Forness, 125 F.2d 928 (2d Cir. 1942), cert. denied, sub nom. City of Salamanca v. United States, 316 U.S. 694.

> "...some of the findings made by the district court are not supported by the evidence and not substantially in accord with the opinion. Such a result can usually be avoided by following what we believe is the better practice of filing findings with the opinion, when the evidence is still fresh in the mind of the trial judge..." 125 F.2d at 942.
>
> * * *
>
> "We stress this matter because of the grave importance of fact-finding. The correct finding, as near as may be, of the facts of a law suit is fully as important as the application of the correct legal rules to the facts as found. An impeccably 'right' legal rule applied to the 'wrong' facts yields a decision which is as faulty as one which results from the application of the 'wrong' legal rule to the 'right' facts. The latter type of error, indeed, can be corrected on appeal. But the former is not subject to such correction unless the appellant overcomes the heavy burden of showing that the findings of fact are 'clearly erroneous.'" 125 F.2d at 942.
>
> * * *
>
> "[22] It is sometimes said that the

> requirement that the trial judge file findings of fact is for the convenience of the upper courts. While it does serve that end, it has a far more important purpose--that of evoking care on the part of the trial judge in ascertaining the facts. For, as every judge knows, to set down in precise words the facts as he finds them is the best way to avoid carelessness in the discharge of that duty: Often a strong impression that, on the basis of the evidence, the facts are thus-and-so gives way when it comes to expressing that impression on paper." 125 F.2d at 942.

An even more serious question is raised by the generalized findings apparently made by the District Judge and relied upon heavily by the landlords in these and other proceedings. To the extent that the District Judge made findings of fact he has apparently exceeded the scope of his appellate review. As is provided in Rules of Bankruptcy Procedure, 810:

> "Upon an appeal the district court may affirm, modify or reverse a referee's judgment or order, or remand with instructions for further proceedings. The court shall accept the referee's findings of fact unless they are clearly erroneous, and shall give due regard to the opportunity of the referee to judge of the credibility of the witnesses."

Prior to the enactment of this Rule, a reviewing District Judge could receive further evidence (General Order 47), and indeed did so in Carter v. Kubler, 320 U.S. 243, 248 (1943), a markedly distinguishable and dated case

mistakenly relied upon by some landlords. In the instant case, the District Court did not receive evidence, nor could it do so.

Yet, the District Judge evidently made three critical findings at variance with the observations of the trier of the facts. The District Judge apparently made a finding that the debtors made promises "with an intention to deceive". (15). The Bankruptcy Judge made no such finding. Similarly, the District Judge found that the debtors' conduct was inequitable even though the Bankruptcy Judge did not so find. The District Judge found that the windfall was illusory. The Bankruptcy Judge noted a clear windfall.

Even if the District Judge had the authority to make new findings, his generalized findings suffer from the same lack of specificity as those of the Bankruptcy Judge.

Viewed in their most favorable light, the District Judge's factual findings apply, in his own words, to "many of the landlords." (15) "Many" is not "all". Thus, by implication, there are at least some landlords who were not victimized by this supposedly inequitable pattern. But who are they, and who are the ones who were not aggrieved? The very identity of the litigants has not been specified, no less the specific facts applicable to each one. The District

Judge goes on to state, in a footnote, that "several " landlords had to borrow money and a 'few' warehouses were sold at tax sales. (17). Again, which landlords suffered and which did not? In effect, the alleged inequitable patterns by the debtors with respect to "many", "several" and a "few" landlords, has been ascribed by the District Judge to them all.

POINT II

THE LANDLORDS HAVE FAILED TO ESTABLISH THAT THE COLUMBUS 3 AND DENVER 4 LEASES WERE TERMINATED PRIOR TO THE COMMENCEMENT OF THE BANKRUPTCY PROCEEDINGS.

The landlords of Columbus 3 and Denver 4 do not rely on the bankruptcy default provision and contend that their leases were terminated prior to the commencement of bankruptcy proceedings by reason of pre-petition defaults in payment of rent and other monetary obligations.

Columbus 3

This proceeding is discussed at pages 25-29 of the brief of the Receiver-Appellant. As appears therein, it is clear that under Ohio law forfeiture would not be allowed, nor was any action commenced by the landlord in Ohio to declare the lease terminated. The landlord of Colmbus 3 purported to terminate the lease without first giving the debtor a 30-day default notice as required under the lease and

without making a prior demand for payment. Moreover, the Ohio courts have not allowed forfeiture even where the requisite notice and demand have been given, holding instead that equity regards the provision for forfeiture as mere security for the payment of the arrears.

The landlord cites no authority for his contention that the lease was validly terminated under Ohio law. The landlords presume to discuss the issue at pages 34 and 41 of their brief. (Page 41 of the landlords' brief follows page 34 with the intervening pages consisting of excerpts from post-trial memoranda submitted to the Bankruptcy Judge. In other words, to follow the argument the reader must turn from page 34 to page 41.)

The only case cited on pages 34 and 41 of the landlords' brief is Audubon Commercial Area Co. v. Skelly Oil Co., 286 F.Supp. 883 (D.Col.1967). The Audubon case was cited by the Receiver-Appellant as authority in connection with the Denver 4 proceeding and the landlords cite that case in an effort to distinguish it with respect to Denver 4. The Audubon case, involving Colorado law, has no bearing on the law of Ohio and the Columbus 3 proceeding. The landlord of Columbus 3 cites no authority whatsoever in support of his contention that the lease terminated under Ohio law and thus

concedes, on this appeal, that the Columbus 3 lease was not terminated.

There was no discussion or even an acknowledgement of the applicability of Ohio law to this proceeding by either of the lower courts and both the Bankruptcy Judge and the District Judge erred in concluding that the Ohio lease was terminated prior to the commencement of the bankruptcy proceedings.

Denver 4

This proceeding is discussed at pages 30-37 of the Brief of Receiver-Appellant. As appears therein, the Colorado courts frown on forfeiture and strictly construe forfeiture provisions in leases against the party seeking to invoke them. Murphy v. Traynor, 135 P.2d 230, 231 (1943).

The lease at bar provides that before the landlord can invoke the termination clause for non-payment, a 30-day notice of default must be given. The landlord does not dispute this and on page 36 of the landlords' brief the 30-day notice requirement is set forth.

The landlord of Denver 4 purported to terminate the lease without giving the requisite 30-day notice and thereby affording the debtor an opportunity to cure.

Again, the landlord does not claim the required

30-day notice was given. By reason of the foregoing there has been no termination of the Ohio lease.

The Ohio courts have held that even where a lease does not expressly provide for a default notice as a prerequisite to termination, the courts will require a prior demand as a condition precedent to the bringing of a termination action. Audubon Commercial Area Co. v. Skelly Oil Co., 268 F. Supp. 883 (D.Col. 1967).

The only argument made by the Denver 4 landlord on the question of termination consists of a tortured attempt to distinguish Audubon. (See page 34, and immediately thereafter page 41, of landlords' brief.)

Landlord contends that Audubon involved the payment of rent whereas in Denver 4 the landlord sought termination on the basis of a default in a payment to the mortgagee. In fact, the landlord sought termination on the basis of a rent default as well as a mortgage default, and by the landlord's own admission the mortgage payments constitute "additional rent" under the lease. (Landlords' brief, p. 42).

Audubon is clearly applicable to the case at bar. However, even if it were not, the dispositive fact is that the Denver 4 landlord failed to give the 30-day default notice expressly required under the terms of the lease. The landlord's attempt to terminate the Denver 4 lease was

thus fatally defective and no authority to the contrary is cited.

There was no discussion or even an acknowledgement of the applicability of Colorado law to this proceeding by either of the lower courts and both the Bankruptcy Judge and the District Judge erred in concluding that the Denver 4 lease terminated prior to the commencement of the bankruptcy proceedings.

CONCLUSION

Landlord mistakenly relies upon Forness, supra, to support his argument that the "unclean hands" doctrine bars equitable relief in these proceedings. In the Forness case the landlord was the exploited Seneca Indian Nation. The tenants, for more than eight years, "cavalierly ignored their modest rent obligation...perhaps out of sheer defiance of a historically maltreated people." 125 F.2d at 940 (Emphasis added).

This Court characterized the defaulting tenants' position in Forness as "an astonishing claim of a vested right in wrongdoing, preventing any correction of an evil condition..." 125 F.2d at 940.

It is against the foregoing background that this Court declined to apply the traditional rule that equity will

relieve tenants from lease forfeiture. The wilful and deliberate exploitation of a "historically maltreated people" was what barred equitable relief in Forness. There can be no equation between the deliberate and repeated acts of the tenants in Forness and the unsuccessful efforts of the debtor-tenants in these proceedings to pay their debts.

Moreover, in the context of a bankruptcy proceeding not only the rights of the debtor-tenant and his landlord are involved. Of equal importance is the position of the other general unsecured creditors.

> "THE REFEREE: ...I think you ought not to overlook that the purpose of this Chapter XI is as much to rehabilitate the debtor as it is to benefit his creditors..." (F-40).

And as this Court noted in Queens Boulevard:

> "The purpose of a Chapter XI arrangement... is to preserve a viable business enterprise where possible and especially when that will be in the 'best interests of...creditors.' 11 U.S.C. § 766 (1970)... we must consider not only the interests of landlord but also those of the debtor and its creditors... Enforcement of the forfeiture...would needlessly injure trade creditors and those outside investors who have furnished capital which has resulted in Queens' rehabilitation. In our view, these individuals stand on no less significant a footing than did the shareholders of the debtors in Weaver and Fleetwood." Queens Boulevard at 4121-22 (Emphasis added).

In conclusion, the opinion of the lower courts with respect to Columbus 3 and Denver 4 should be reversed on the law.

The opinion of the lower courts with respect to Buffalo 2 and Miami 7 should likewise be reversed or alternatively, remanded for special findings of fact and separate conclusions of law.

Respectfully submitted,

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November 14, 1974.

STATE OF NEW YORK
COUNTY OF NEW YORK

BERT MYERS being duly sworn deposes and says: On November 14th (REPLY), 1974 I served the within ~~record on appeal~~ brief ~~appendix~~ on Levy Levy & Ruback the attorney for the ~~respondent~~ Debtors-Appellants by leaving ~~mailing~~ (two) ~~three~~ copies thereof at his office located at 225 Broadway New York, N.Y.

Bert Myers

Sworn to before me this 14th day of November 1974

Mary Casella
Notary Public

MARY CASELLA
Notary Public, State of New York
No. 31-0592250
Qualified in New York County
Commission Expires March 30, 1975

STATE OF NEW YORK
COUNTY OF NEW YORK

JOE SANTIAGO being duly sworn deposes and says: On November 14th (REPLY), 1974 I served the within ~~record on appeal~~ brief ~~appendix~~ on Hahn Hessen Margolis & Ryan (appellees) the attorney for the ~~respondent~~ Landlords of Buffalo 2, Columbus 3 Dinner & Miami 7-9 by leaving ~~mailing~~ (two) ~~three~~ copies thereof at his office located at 350 Fifth Avenue New York, N.Y.

Joe Santiago

Sworn to before me this 14th day of November 1974

Mary Casella
Notary Public

MARY CASELLA
Notary Public, State of New York
No. 31-0592250
Qualified in New York County
Commission Expires March 30, 1975